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In the Supreme Court of the United States

OCTOBER TERM, 1955

No. 146

THE AMERICAN METAL COMPANY, LIMITED, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 272a-286a; Pet. A-18-A-30) are reported at 19 T.C. 879. The opinion of the Court of Appeals (Pet. A-3-A-17) is reported at 221 F.2d 134.

JURISDICTION

The judgment of the Court of Appeals was entered on March 15, 1955. (Pet. A-1-A-2.) The petition for a writ of certiorari was filed June 13, 1955.

The jurisdiction of this Court rests upon 28 U.S.C., Sec. 1254.

QUESTION PRESENTED

Whether the production taxes imposed under the Mexican Mining Tax Laws and paid by Minera, taxpayer's Mexican subsidiary, in the years 1924 through 1947, were income taxes or taxes paid by Minera in lieu of income taxes within the meaning of Section 131 of the Internal Revenue Code of 1939, so as to entitle taxpayer to a foreign tax credit for the payment of such taxes by Minera.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code of 1939:

> SEC. 131. TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES.
>
> (a) [as amended by Sec. 158(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Allowance of Credit.*—If the taxpayer chooses to have the benefits of this section, the tax imposed by this chapter, except * * *, shall be credited with:
>
> (1) *Citizens and domestic corporations.*—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and
>
> * * * * *
>
> (f) [as amended by Sec. 158(e) of the Revenue Act of 1942, *supra*, and Sec. 130(b) of the Revenue

Act of 1943, c. 63, 58 Stat. 21] *Taxes of Foreign Subsidiary.*—

(1) *Foreign subsidiary of domestic corporation.*—For the purposes of this section, a domestic corporation which owns a majority of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of any income, war-profits, or excess-profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States, upon or with respect to the accumulated profits of such foreign corporation from which such dividends were paid, which the amount of such dividends bears to the amount of such accumulated profits. The term "accumulated profits" when used in this subsection in reference to a foreign corporation, means the amount of its gains, profits, or income in excess of the income, war-profits, and excess-profits taxes imposed upon or with respect to such profits or income; * * *.

* * * * *

(h) [as added by Sec. 158(f) of the Revenue Act of 1942, *supra*] *Credit for Taxes in Lieu of Income, Etc., Taxes.*—For the purposes of this section and section 23(c)(1), the term "income, war-profits, and excess-profits taxes" shall include a tax paid in lieu of a tax upon income, war-profits, or excess-

profits otherwise generally imposed by any foreign country or by any possession of the United States.

* * * * *

(26 U.S.C. 1952 ed., Sec. 131.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

> SEC. 29.131-2. *Meaning of Terms.*—The term "amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year" means taxes proper (no credit being given for amounts representing interest or penalties) paid or accrued during the taxable year on behalf of the taxpayer claiming credit. For the purposes of section 131 and section 23(c)(1) the term "income, war-profits, and excess-profits taxes" includes a tax imposed by statute or decree by a foreign country or by a possession of the United States if (a) such country or possession has in force a general income tax law, (b) the taxpayer claiming the credit would, in the absence of a specific provision applicable to such taxpayer, be subject to such general income tax, and (c) such general income tax is not imposed upon the taxpayer thus subject to such substituted tax. For example, the A Corporation does business in the X country, which imposes an income tax upon substantially a net income base. The ascertainment of net income, though not the determination of gross income, from

sources in X country is found administratively difficult. The X country, by decree, provides that corporations circumstanced as was the A Corporation would, in lieu of the income tax at the rate of 20 percent otherwise payable, be subject to tax at the rate of 10 percent upon the amount of gross income from X country. In accordance with such decree, the A Corporation paid X country the sum of $25,000 in 1943 with respect to its tax liability to the X country for the year 1942. Such amount, subject to the applicable limitations, is available as a credit to the A Corporation as foreign income, war-profits, or excess-profits taxes against the United States tax liability for the year 1942.

* * *

STATEMENT

The Tax Court made detailed findings of fact (R. 274a-280a; Pet. A-19-A-24) based largely on a detailed stipulation of facts (R. 13a-92a). For present purposes the facts may be summarized as follows:

Taxpayer is a New York corporation which owns a majority of the stock of Compania Minera de Penoles, S. A. (hereinafter called Minera), a Mexican corporation engaged, in Mexico, in the business of mining, milling, smelting and refining non-ferrous metals directly and through subsidiaries. In August 1947 Minera paid a taxable dividend to its shareholders, in the amount of $8,250,000, out of its earnings and profits accumulated since 1924. Tax-

payer received $8,110,932.50 of the dividend distribution. In its consolidated income tax return for the calendar year 1947, taxpayer chose to take the foreign tax credit authorized by Section 131 of the Internal Revenue Code of 1939 for foreign income taxes paid by a subsidiary on the earnings and profits distributed to the parent. The credit was claimed by taxpayer in an amount which covered taxes paid by Minera during the years 1924 through 1947 under the Mexican *Income* Tax Laws and also production taxes paid under the Mexican *Mining* Tax Laws. The Commissioner disallowed the portion of the claimed credit attributable to the production taxes paid by Minera under the Mexican *Mining* Tax Laws, on the ground that such taxes were not income taxes or taxes paid in lieu of income taxes within the meaning of Section 131 of the Code. (R. 13a-17a, 29a-31a, 33a, 274a-275a.)

The nature of the Mexican *Income* Tax Laws, as well as the amounts paid by Minera thereunder for each of the years 1924 through 1947, is reflected in the Tax Court's findings of fact (R. 277a-278a; Pet. A-22-A-23; see, also, R. 33a, 92a) and will not be restated here.[1] The production taxes paid by Minera under the Mexican *Mining* Tax Laws, for which credit has been disallowed, were deductible and were deducted by Minera in computing its taxable income under the Mexican *Income* Tax Laws for each of the years 1924 through 1947. (R. 25a-26a, 275a; Pet. A-21.)

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[1] The provisions of the Mexican Income Tax Laws are reflected in Exhibit 7-G (see R. 27a-28a), which is not contained in the printed record.

The Republic of Mexico owns all mineral in place within the Republic and all mining of those minerals is through concessions from the Government. The concessions are granted without consideration but the Government has attempted to require the concessions to be worked or forfeited. (R. 275a-276a; Pet. A-21.)

The Mexican *Mining* Tax Laws in effect from 1924 to 1947 (R. 26a, 27a) contained provisions similar to the Mining Tax Law of August 30, 1934 (R. 277a; Pet. A-22), which is contained in the record at pages 35a-57a.[2] Chapter III of that law (R. 37a-42a), relating to the production taxes for which credit has been disallowed, imposed tax on the production in Mexico of metals, metallic compounds for industrial uses and non-metallic ores. The tax was imposed at fixed rates on the value of the metals and metallic compounds as determined monthly on the basis of the averages of the New York market prices and the sight exchange between the dollar and the Mexican currency. The rates at which the tax was imposed were highest on virgin ores and declined through the various steps involved in producing the refined metal, on which the rate was lowest. The rates on silver, for example, declined in one per cent stages from six per cent on virgin ores to three per cent on refined silver, but increased one percent for each increase of five cents in the value of silver, over

[2] The other Mexican Mining Tax Laws are not contained in the printed record, although English translations thereof were exhibits to the stipulation of facts.

forty cents per troy ounce, on the New York market. (R. 276a-277a; Pet. A-21-A-22.)

The production taxes were imposed upon the extraction of ore by the miner from the mineral deposit in Mexico. The products generally had to be delivered by their holders for payment of the production tax within 30 days following their production unless they were to be subjected to further treatment in Mexican plants, in which case the production tax was payable when the further processing in Mexico was completed. Payment of the production tax was due at the time of export if the product was exported prior to final treatment. The production tax was less if the treatment of the material was carried to completion in Mexico than it was if the material was exported before final treatment. Discounts on production taxes were allowed on the lower grade ores and on all ores mined during the first few years from a new mine or during the first few years from a reopened mine which had not been operated during the ten previous years. (R. 276a; Pet. A-21.)

The department of the Ministry of Finance which administered the production taxes was entirely separate from the department of the Ministry of Finance which administered the Mexican Income Tax Laws. (R. 279a.)

The Tax Court held that the Mexican production taxes were not income taxes or taxes paid in lieu of income taxes within the meaning of Section 131 of the Code. (R. 280a-285a; Pet. A-25-A-29.) The Court of Appeals affirmed. (Pet. A-4-A-15.)

ARGUMENT

As reasons for granting the writ, taxpayer asserts that the decision below presents an important question which should be settled by this Court and that the court below has misinterpreted and misapplied decisions of the Court. (Pet. 11-21.) Both assertions are incorrect.

1. Contrary to taxpayer's argument (Pet. 11-15), there is no unsettled question as to the standard to be applied in determining the types of foreign taxes entitled to credit under Section 131 of the Internal Revenue Code of 1939, *supra*, pp. 2-4. The statute itself fixes the types of taxes entitled to credit by authorizing the credit for the payment of "income * * * taxes" (Section 131 (a)(1) and (f)(1)). This includes, as declared in subsection (h), "a tax paid in lieu of a tax upon income * * * otherwise generally imposed by any foreign country * * * " (Section 131(h)). The standard for determining what constitutes "income * * * taxes" for the purpose of Section 131 is set forth in this Court's decision in *Biddle* v. *Commissioner*, 302 U.S. 573, where it was stated (p. 579) that the phrase "income taxes paid" in Section 131 must be interpreted according to its meaning as used in our own revenue laws. Thus, whether the taxpayer there had paid the tax was held to depend upon whether his actions in conformity with foreign law were "the substantial equivalent of payment of the tax as those terms are used in our own statute." (*ibid.*) Following that decision, the lower courts, as in the present

case (see Pet. A-8), have properly and consistently held that, in determining whether a foreign tax is an income tax for the purposes of Section 131, the controlling criterion is whether the foreign tax is the substantial equivalent of an income tax as that term is understood in the United States. See *Keasbey & Mattison Co.* v. *Rothensies,* 133 F. 2d 894, 897 (C.A. 3d), certiorari denied, 320 U.S. 739; *New York & H. Rosario Min. Co.* v. *Commissioner,* 168 F. 2d 745, 747 (C.A. 2d); *Northwestern Mut. F. Ass'n* v. *Commissioner,* 181 F. 2d 133 (C.A. 9th); *St. Paul Fire & Marine Ins. Co.* v. *Reynolds,* 44 F. Supp. 863 (D. Minn.). The standard for determining what constitutes "a tax paid in lieu of a tax upon income" is stated in Section 29.131-2 of Treasury Regulations 111, *supra,* pp. 4-5, which is expressive of the Congressional purpose in enacting subsection (h). See S. Rep. No. 1631, 77th Cong., 2d Sess., p. 131 (1942-2 Cum. Bull. 504, 602).

More precise standards, even if feasible, are not required as a guide to decision in the present case, for the Mexican production tax clearly does not meet the United States concept of an income tax. Under our revenue laws a tax on income is a tax on gains and profits, as the courts have held in applying Section 131. *Keasbey & Mattison Co.* v. *Rothensies,* 133 F. 2d 894, 897 (C.A. 3d), certiorari denied, 320 U.S. 739; *Northwestern Mut. F. Ass'n* v. *Commissioner,* 181 F. 2d 133, 135 (C.A. 9th); *St. Paul Fire & Marine Ins. Co.* v. *Reynolds,* 44 F. Supp. 863, 865 (Minn.). As applied to mining operations, which resemble a manufacturing busi-

ness carried on by the use of the soil and are treated as income-producing operations, our income tax is imposed on the miner's net profits, consisting of gross proceeds less allowable deductions. See *Anderson* v. *Helvering*, 310 U.S. 404; *Burnet* v. *Harmel*, 287 U.S. 103. Contrariwise, the Mexican production tax is imposed on the production of metals; it is measured by the value of the metals produced; and it attaches when the ore is extracted from the subsoil irrespective of whether any profit results and even irrespective of whether the metal is subsequently sold. Thus, the Mexican production tax, instead of being a tax on income within the United States concept, falls into the classification of a privilege tax (see *Oliver Iron Co.* v. *Lord*, 262 U.S. 172; *Hope Gas Co.* v. *Hall*, 274 U.S. 284). It is measured by the value of the metal mined and, as the court below held (Pet. A-9-A-11), is a condition of extracting ore which belongs to the Republic of Mexico.

2. Taxpayer argues (Pet. 16-21) that the court below erred in giving weight to decisions of this Court holding that a privilege tax measured by income is not an income tax. See, *e.g.*, *Flint* v. *Stone Tracy Co.*, 220 U.S. 107, 162, 163-164; *McCoach* v. *Minehill Railway Co.*, 228 U.S. 295, 306-308; *Stratton's Independence* v. *Howbert*, 231 U.S. 399, 414; *Anderson* v. *Forty-Two Broadway Co.*, 239 U.S. 69, 72.[3] The suggestion is that these cases

[3] The court below did not cite those cases but apparently included them in the reference (Pet. A-10) to *Keasbey &*

are inapposite for purposes of determining availability of foreign tax credit because they are based on a "subject" and "measure" analysis "founded in constitutional necessities" (Pet. 17). But certainly a decision as to the nature of a tax is not lacking in persuasiveness because the question arose in the context of a constitutional challenge to the taxing power.[4] As pointed out above, it is the United States concept of the nature of the tax which is controlling under Section 131.

In any event, so far as the Mexican production tax is concerned, there is no occasion for debate as to the soundness of the "subject" and "measure" distinction. There is no conceptual problem here, for income is neither the subject nor the measure of the tax. The tax has relation to income only in the vague sense that, as the court below stated (Pet. A-12), the rate of the tax varies with a factor which affects the prosperity of the mining industry generally. As the court below also stated, the Mexican production tax is more clearly and certainly a privilege tax than the Quebec tax held to be a privilege tax in *Keasbey & Mattison Co.* v.

Mattison Co. v. *Rothensies*, 133 F. 2d 894 (C. A. 3d), certiorari denied, 320 U. S. 739, as a case which "cites numerous cases which lend still further support to our conclusion."

[4] *Interstate Pipe Line Co.* v. *Stone*, 337 U. S. 662, *Spector Motor Service* v. *O'Connor*, 340 U. S. 602, and *Railway Express Agency* v. *Virginia*, 347 U. S. 359, cited by petitioner (Pet. 17-18), involved the impact of state privilege taxes on interstate commerce and in nowise detracted from the Court's prior holdings that a privilege tax is not an income tax.

Rothensies, 133 F. 2d 894 (C.A. 3d), certiorari denied, 320 U.S. 739.

CONCLUSION

The decision below is clearly correct and in full accord with the decisions of this Court. There is no conflict among the circuits. The petition for a writ of certiorari should be denied.

Respectfully submitted,

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JULY 1955.

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